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# ► Policy design of the employment adjustment subsidy in Japan

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# ▶ **Policy design of the employment adjustment subsidy in Japan**

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Ippei Tsuruga

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## ▶ 1. Introduction

This paper aims to review and summarize the feature and design of the Employment Adjustment Subsidy (*Koyou Chousei Joseikin*) in Japan in order to contribute to discussions in Indonesia about policy designs on unemployment protection.

The employment insurance system in Japan consists of Unemployment Benefits and the Employment Insurance Services, as stipulated by the Employment Insurance Act, 1974 (article 3)<sup>1</sup>. The Employment Insurance Services play a core role in active labour market policies (ALMPs), which consist of employment stabilization programmes and human resource development programmes, and aim at enhancing enterprises' capacity and resilience through subsidies, and thereby restrain expenditures of Unemployment Benefits. While Unemployment Benefits are financed through contributions from workers and employers as well as general tax revenues, the Employment Insurance Services are financed solely by employers because the direct beneficiaries of the services are enterprises.

The employment stabilization programmes incentivize employers to maintain employment – especially in economic downturns – through the Employment Adjustment Subsidy. The Labour Standards Act, 1947<sup>2</sup> (article 26) primarily obliges an employer to pay an employee leave compensation of 60 per cent or more of the employee's average daily wage for the last three months<sup>3</sup>, when the enterprise reduces business activities due to any reasons attributable to the employer. The Employment Adjustment Subsidy reimburses part of the amount an employer paid in leave compensation, subject to the employer's commitment to continued employment after a temporary reduction or suspension of business. By creating a solidarity fund among employers, the subsidy aims to maintain employment by reducing the financial burden faced by employers with regard to the payment of leave compensation.

### Programmes and financing of the Employment Insurance System

| Programme                     |                                       | Finance              |                      |                         |
|-------------------------------|---------------------------------------|----------------------|----------------------|-------------------------|
|                               |                                       | Finance              | Employer             | Government              |
| Unemployment Benefits         | Jobseekers' benefits                  | 0.3 per cent of wage | 0.3 per cent of wage | 2.5 per cent of payment |
|                               | Employment promotion benefits         |                      |                      |                         |
|                               | Education and training benefits       |                      |                      |                         |
|                               | Continuous employment benefits        |                      |                      |                         |
| Employment Insurance Services | Employment stabilization programmes   | n/a                  | 0.3 per cent of wage | n/a                     |
|                               | Human resource development programmes |                      |                      |                         |

n/a = not applicable.

<sup>1</sup> Available (in Japanese) at [https://elaws.e-gov.go.jp/search/elawsSearch/elaws\\_search/lsg0500/detail?lawId=349AC000000116](https://elaws.e-gov.go.jp/search/elawsSearch/elaws_search/lsg0500/detail?lawId=349AC000000116).

<sup>2</sup> Available (in Japanese) at [https://elaws.e-gov.go.jp/search/elawsSearch/elaws\\_search/lsg0500/detail?lawId=322AC000000049](https://elaws.e-gov.go.jp/search/elawsSearch/elaws_search/lsg0500/detail?lawId=322AC000000049).

<sup>3</sup> Please note that the Labour Standards Act, 1947, uses the term "average wage" to refer to the average daily wage received by workers. This report follows the terminology used in the Act. See box 1 below for more on how the average wage is determined.

▶ **Box 1**▶ **Defining average wage and minimum compensable amount****(1) Average wage**

The average wage used to calculate the amount of leave compensation due to an employee is defined as the total amount of paid wages for the last three months (prior to the first day of leave) divided by the number of calendar days in those months (Labour Standards Act, article 12). For instance, if an enterprise pays salaries at the 20th of each month and calculates a particular employee's average wage following the table below on June 10, the average wage for that employee is 7,415 Japanese yen. If this person's employment is suspended for reasons attributable to the employer, the employee should be paid at least 60 per cent of this amount for each day of the leave period.

| <b>Paid month and period of services</b> | <b>March<br/>Feb. 21 – Mar. 20</b>    | <b>April<br/>Mar. 21 – Apr. 20</b> | <b>May<br/>Apr. 21 – May. 20</b> |
|--|---------------------------------------|------------------------------------|----------------------------------|
| Basic salary                             | 200 000                               | 200 000                            | 200 000                          |
| Transport allowance                      | 10 000                                | 10 000                             | 10 000                           |
| Overtime                                 | 10 000                                | 20 000                             | 0                                |
| Monthly total                            | 220 000                               | 230 000                            | 210 000                          |
| Total paid wage                          | 220 000 + 230 000 + 210 000 = 660 000 |                                    |                                  |
| Total calendar days                      | 28 + 31 + 30 = 89                     |                                    |                                  |
| Average wage                             | 660 000/89 = 7 415.73                 |                                    |                                  |

**(2) Minimum compensable amount**

In some instances, the average wage calculated for an employee might be less than the minimum compensable amount. Such a scenario might arise in the case of affected workers who were being paid on an hourly, daily or performance basis for the last three months. The minimum compensable amount is defined as the total amount of payments for the last three months divided by the number working days – instead of calendar days – multiplied by 60 per cent. For instance, consider an enterprise that pays wages on the 25th of each month and calculates an employee's average wage on February 5. The table below presents an employee who earns 8,000 yen for basic salary and 400 yen for transport per day, but who only worked 35 days during the previous three months. Using the formula above, the average wage for the three months would come to 3,195 yen. However, the minimum compensable amount for a worker who only worked 35 days is 5,040 yen. In this case, the latter minimum compensable amount will be referenced for calculating the Employment Adjustment Subsidy – that is, the worker must receive at least 60 per cent of the minimum compensable amount per day of leave.

| Paid month and period of services | November<br>Oct. 26 – Nov. 25        | December<br>Nov. 26 – Dec. 25 | January<br>Dec. 26 – Jan. 25 |
|-----------------------------------|--------------------------------------|-------------------------------|------------------------------|
| Basic salary                      | 120 000                              | 40 000                        | 120 000                      |
| Transport allowance               | 6 000                                | 2 000                         | 6 000                        |
| Overtime                          | 126 000                              | 42 000                        | 126 000                      |
| Monthly total                     | 126 000 + 42 000 + 126 000 = 294 000 |                               |                              |
| Total paid wage                   | 31 + 30 + 31 = 92                    |                               |                              |
| Total calendar days               | 15 + 5 + 15 = 35                     |                               |                              |
| Total calendar days               | 294 000/92 = 3 195.65                |                               |                              |
| Average wage                      | 294 000/35 x 0.6 = 5 040             |                               |                              |

In such a case, if an employer previously agreed to 15 working days with the worker between January 26 and February 25, but then decided to reduce it to 14 working days, the employer still has to pay at least 60 per cent of minimum compensable amount for one day, which is 3,024 yen (5,040 x 0.6), and salary for 14 working days.

Source: Osaka Labour Bureau 2016; Osaka Prefectural Government 2020; Labour Standards Act, 1947.

## ▶ 2. Design

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The Employment Adjustment Subsidy is typically applied for three types of scenarios, including when:

- ▶ enterprises reduce working hours of employees due to temporary closure or restructure of business activities;
- ▶ enterprises provide employees with education and training opportunities; and
- ▶ enterprises second employees to other companies, as stipulated in the Enforcement Regulation of the Employment Insurance Act (article 102-2)<sup>4</sup>.

This paper is focused on the subsidy for the case of temporary reduction or restructure of business activities.

### 2.1 Coverage

Because the Employment Adjustment Subsidy is part of the Employment Insurance package, its coverage follows that of the Employment Insurance. Therefore, the subsidy covers employees who work for at least 20 hours per week and have contracts of more than one month's duration<sup>5</sup>. Employees have to have accumulated contributions to the Employment Insurance for at least the past six months<sup>6</sup>, which is set at the same level as unemployment cash benefits for involuntarily unemployed workers.

As the subsidy aims at maintaining employment, employers will not be reimbursed for employees who:

- ▶ voluntarily resign due to the employment adjustments;
- ▶ are not willing to work; and
- ▶ are not capable of working.<sup>7</sup>

### 2.2 Qualifying conditions

As outlined above, the Employment Adjustment Subsidy is, in principle, aimed at enterprises that have made temporary employment adjustments as a result of reduced business activity. These enterprises must be seeking to maintain employment, and have paid leave compensation to affected employees.<sup>8</sup>

In addition, the subsidy has set further, more detailed eligibility criteria to operationalize these principles. Some of the major criteria include:

- ▶ Leave applied for all employees is longer than one day, or for specified employees for at least one hour;
- ▶ Leave compensation has been paid at an equivalent of at least 60 per cent of employees' average wage over the previous three months;<sup>9</sup>

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<sup>4</sup> Available (in Japanese) at [https://elaws.e-gov.go.jp/search/elawsSearch/elaws\\_search/lsg0500/detail/350M50002000003\\_20180101\\_429M60000100066/0?revIndex=4&lawId=350M50002000003&openerCode=1](https://elaws.e-gov.go.jp/search/elawsSearch/elaws_search/lsg0500/detail/350M50002000003_20180101_429M60000100066/0?revIndex=4&lawId=350M50002000003&openerCode=1).

<sup>5</sup> Employment Insurance Act, article 6.

<sup>6</sup> Enforcement Regulation of the Employment Insurance Act, article 102-3.

<sup>7</sup> The subsidy does not reimburse employers for amounts paid to workers who went on strike. These employees are regarded as workers who are not willing or available to work. Similarly, employees who are on sick leave cannot be considered by the subsidy because they do not have the capacity to work.

<sup>8</sup> Enforcement Regulation of the Employment Insurance Act, article 102-3.

<sup>9</sup> Enforcement Regulation of the Employment Insurance Act, article 102-3.

- ▶ Average revenue or production over the last three months dropped by 10 per cent or more compared to the same period in the previous year;
- ▶ Over the last three months the average number of insured employees and dispatched workers has not increased by more than 10 per cent or four workers or more for small- and medium-sized enterprises (SMEs), or by 5 per cent or 6 workers or more for large enterprises compared to the same period in the previous year (see box 2); and
- ▶ The submission of a collective agreement with employees regarding the implementation plan for temporary closure or reduced business activities.

It should be noted that the subsidy assesses not only contribution records and economic and employment performance, but also industrial relations. While employers are primarily liable for leave compensation, the subsidy contributes to encouraging employers to engage in dialogue and to collaborate with employees to maintain employment and overcome challenging times for the business.

## ▶ Box 2

### Defining small- and medium-sized enterprises

The Employment Adjustment Subsidy provides SMEs with greater assistance because they and their employees are more vulnerable to economic shocks. The subsidy considers the size of capital held and number of employees to define SMEs or large enterprises.

| Industry                      | Capital                 | Number of employee |
|-------------------------------|-------------------------|--------------------|
| Retail (including restaurant) | 50 million yen or less  | 50 or less         |
| Services                      | 50 million yen or less  | 100 or less        |
| Wholesale                     | 100 million yen or less | 100 or less        |
| Other industries              | 300 million yen or less | 300 or less        |

Source: Enforcement Regulation of the Employment Insurance Act, Article 102-3.

## 2.3 Benefit level

As discussed above, employers have to pay employees at least 60 per cent of their average wage over the previous three months in the form of leave compensation. Upon submission and approval of an employer application, the Employment Adjustment Subsidy will reimburse the employer for a portion of the incurred expenditure. The subsidy amounts are set at equivalent amounts of two thirds of leave compensation expenditure for SMEs, and one half for large enterprises (see box 3).

## ▶ Box 3

▶ **Simulating the subsidy amount**

The table below simulates the actual financial burden faced by employers for financing leave compensation after they have received the reimbursement from the Employment Insurance fund. Assuming that the average wage in the previous three months and the average insurable earnings in the previous year were the same, and an employer of small enterprise pays their employees 60 per cent of their average wages and claims for the subsidy, the employer will ultimately have financed only 20 per cent of their employees' average wages. The remaining 40 per cent will have been reimbursed by the Employment Insurance fund.

| Financer                      | SMEs                | Large enterprises   |
|-------------------------------|---------------------|---------------------|
| Employment Adjustment Subsidy | 40 per cent of wage | 30 per cent of wage |
| Employer                      | 20 per cent of wage | 30 per cent of wage |

More precisely, in practice, the subsidy amount is calculated based on the daily wage per worker in the previous year multiplied by the replacement rate for leave compensation as stipulated by collective agreement, the subsidy rate and man days of temporary work stoppage.

$$\text{Subsidy amount} = \frac{\text{Total amount of insurable earnings for employment insurance in the last year}}{\text{Monthly average number of insured in the last year} \times \text{Prescribed working days in the last year} \times \text{Replacement rate for leave compensation as stipulated by collective agreement} \times \text{Subsidy rate} \times \text{Man days of temporary work stoppage}}$$

The maximum amount for the subsidy follows that of the unemployment cash benefit, which is 8,330 yen per employee per day, as of March 2020. This also means that the ceiling is indexed with the average wage of the previous year.

## 2.4 Benefit duration

Employers define a period of one year when they plan to make employment adjustments, and can claim the subsidy up to a maximum duration of 100 days in one year or 150 days for three years (see box 4).<sup>10</sup>

**▶ Box 4**

## Calculating the number of days for the subsidy

The subsidy for employers is calculated on a monthly basis. The number of days to be subsidized is defined as the total man-days of absence divided by the total number of employees who are affected by the employment adjustment and who qualify for the subsidy.

For example, provided that ten employees are affected by the employment adjustment and are qualified for the subsidy, and six of them take five days off work at a time, the number of days used for calculating the subsidy would be three ( $= 6 \times 5/10$ ) instead of five ( $= 6 \times 5/6$ ).

Source: Ministry of Health, Labour and Welfare 2020.

## 2.5 Subsequent claim

The subsidy sets a waiting period for employers to make subsequent claims. After the initial year, employers have to wait for at least one year before they can make a second claim and they once again must define another year for employment adjustments. The waiting period for subsequent claim aims at preventing enterprises from depending on the subsidy for an unnecessarily long period.

## 2.6 Application

Prior to the implementation of employment adjustments, employers have to submit their implementation plans to the Prefectural Labour Bureau or Hello Work offices. These plans must include information about the:

- ▶ duration of the employment adjustment
- ▶ number of potentially affected employees
- ▶ justifications for selection of employees and units
- ▶ collective agreement for the implementation plan and
- ▶ other supporting documents to clarify qualifying conditions.

<sup>10</sup> Enforcement Regulation of the Employment Insurance Act, article 102-3.

The agreement between employer and employees has to be signed by a trade union that more than half of employees participate in or by an employee who represents at least half of employees, if there are no corresponding trade unions.

## 2.7 Claim

Employers have to file a claim for the subsidy at the Prefectural Labour Bureau and the Hello Work office within two months after the defined employment adjustment period.<sup>11</sup> For example, if the defined period for the employment adjustment was from April 16 to May 15, the claim period for the subsidy is from May 16 to July 15 (Ministry of Health, Labour and Welfare 2020). If an enterprise goes bankrupt before the decision for the subsidy payment is made, the enterprise will not receive a payment.

## 2.8 Approval

When receiving an application or claim, the Prefectural Labour Bureau or the Hello Work office will verify qualifying conditions. The Prefectural Labour Bureau is the final approver for both applications and claims.

## 2.9 Fraud and penalty

The Prefectural Labour Bureau discloses the name of an employer when it commits fraud to receive the subsidy, and has put several measures in place to minimize risks of abuse.<sup>12</sup> Employers are not eligible for the subsidy if:

- ▶ They have had the subsidy cancelled due to fraud within the last five years.
- ▶ They still have senior management personnel who previously committed fraud.
- ▶ They did not contribute to the Employment Insurance for the previous fiscal year.
- ▶ They violated labour-related laws during the last 12 months.

Appendix I below provides a summary table of the material presented in section two of this report.

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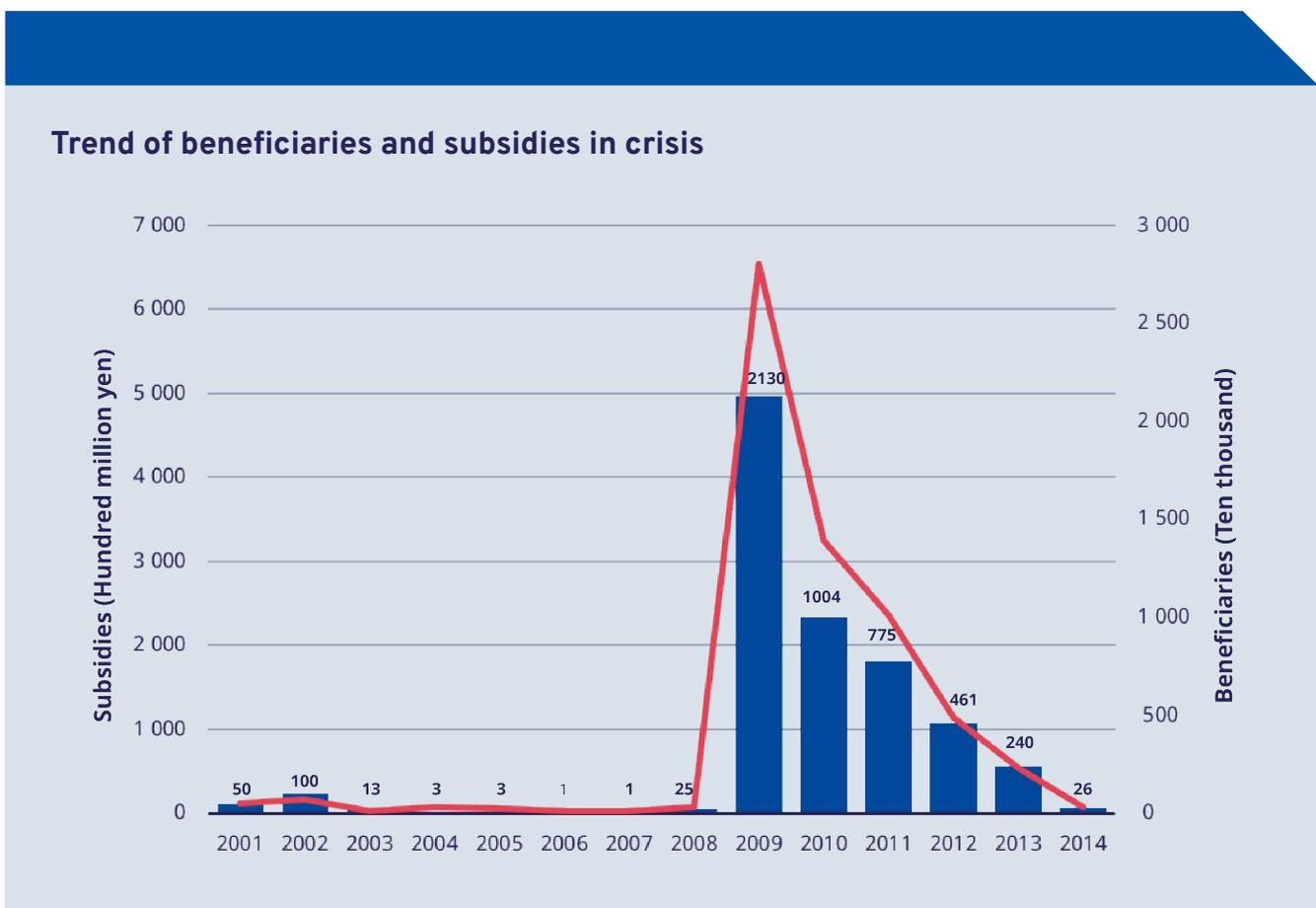
<sup>11</sup> The period is one month, usually defined by a payment cycle (see box 4).

<sup>12</sup> Enforcement Regulation of the Employment Insurance Act, article 120-2.

### ▶ 3. Special measures for crisis response

Looking back to past crisis responses, the Government has implemented special measures at either the regional or national level, depending on the impact of the crisis in question. While the primary responsibility for leave compensation remains with employers, even in a time of crisis, the Government tends to flexibly expand the Employment Adjustment Subsidy by relaxing its conditions and increasing subsidies to reduce economic burdens on employers. After the crisis abates, the Government often adjusts the parameters back so that the Employment Insurance fund can accumulate reserves for future crises.

The common parameters adjusted in a time of crisis include coverage, production, employment, benefit level, benefit duration, waiting period for subsequent claims, and administrative procedures (see Appendix II). An analysis of administrative data related to the Global Financial Crisis and the East Japan Earthquake shows a significant expansion of coverage stemming from the relaxing of conditions related to the economic and employment indicators (Japan Institute for Labour Policy and Training 2017). If the qualifying condition on economic indicators had not been relaxed, only 51.3 per cent of enterprises receiving subsidies in 2009, 18.3 per cent in 2010, 16.8 per cent in 2011, and 14.7 per cent in 2012 would have met the requirement. Similarly, if the qualifying condition on employment indicators had remained in place, only 73 per cent of enterprises receiving subsidies in 2009, 70.7 per cent in 2010, 66.5 per cent in 2011, and 70.5 per cent in 2012 would have met the requirement. These impacts in coverage are observed in the figure below.



Note: The numbers presented in the chart are the total number of monthly beneficiaries. The same workers may be counted several times if they receive benefits for periods longer than one month.

Source: Japan Institute for Labour Policy and Training 2017.

## ▶ Reference

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## ► Appendix I - Key parameters of the Employment Adjustment Subsidy

Leave compensation is paid to employees by employers for at least 60 per cent of previous average wage. Of which expenditure, employers can receive subsidies in accordance with the specified conditions. The table below summarizes conditions for employers to receive subsidies.

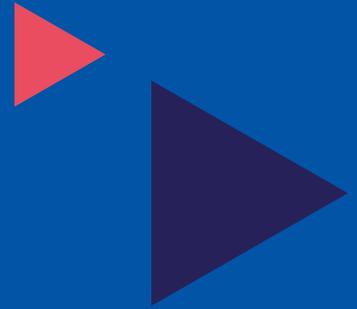
| Parameters                                 |                         | Base design   |   |
|--|-------------------------|---|---|
| <b>Contingency</b>                         |                         | Leaves applied for all employees longer than one day or specified employees for at least one hour because of reduction in business activities.  |   |
| <b>Coverage</b>                            |                         | Employees insured by the employment insurance at least for 6 months. (Employers have to register to the Employment Insurance their employees who work for 20 hours per week and under contracts over 1 month) |   |
| <b>Qualifying condition</b>                | Production indicator    | Production in the last 3 months dropped by 10 per cent or more compared to the same period in the previous year   |   |
|  | Employment indicator    | Large-sized enterprises   | Average number of insured employees and dispatched workers has not increased by more than 5 per cent or by 6 or more workers) in the last 3 months compared to the same period in the previous year |
|  |                         | SMEs  | Average number of insured employees and dispatched workers has not increased by more than 10 per cent or by 4 workers or more in the last 3 months compared to the same period the previous year    |
|  | Leave compensation      | Leave compensation paid to employee(s) at a level of at least 60 per cent of the average wage over the last three months  |   |
|  | Industrial relations    | The submission of employer–employee agreement for the implementation plan for closure or reduced business activities  |   |
| <b>Benefit level</b>                       | Large-sized enterprises | 50% of equivalent amount paid for the leave compensation  |   |
|  | SMEs                    | 67% of equivalent amount paid for the leave compensation  |   |
| <b>Maximum benefit</b>                     |                         | Same as unemployment benefit (8,330 yen per employee per diem in 2020)  |   |
| <b>Indexation of maximum benefit</b>       |                         | Same as unemployment benefit (that is, average wage)  |   |
| <b>Benefit duration</b>                    |                         | 100 days per annum or 150 days for 3 years  |   |
| <b>Waiting period for subsequent claim</b> |                         | 1 year  |   |
| <b>Application</b>                         |                         | Prior to employment adjustment  |   |
| <b>Finance</b>                             |                         | Employment Insurance (0.3 per cent of wage by employers)  |   |
| <b>Disqualified enterprises</b>            |                         | Had the subsidy cancelled due to fraud within the last 5 years.   |   |
|  |                         | Senior management personnel previously committed fraud.   |   |
|  |                         | Not contributed to the Employment Insurance for the previous fiscal years.  |   |
|  |                         | Violated labour-related laws in the last 1 year.  |   |

► Appendix II - Summary of special measures for crisis response

| Parameters                                 |                         | Base design (as of April 2008)  | Response to the Global Financial Crisis (as of June 2009)  | Base design (as of December 2013)  | Response to the COVID-19 Crisis (as of June 2020)   |
|--|-------------------------|---|--|--|---|
| <b>Coverage</b>                            |                         | Employees insured for at least 6 months   | <b>All insured employees (no minimum timeframe)</b>  | Employees insured for at least <b>6 months</b>   | <b>All employees, including workers who are not insured</b>   |
| <b>Qualifying condition</b>                | Production              | Production in the last 6 months dropped by 10% or more compared to the same period in the previous year | Production in the last <b>3 months</b> dropped by <b>5%</b> compared to the previous <b>3 months</b> or the same period in the previous year | Production in the last 3 months dropped by <b>10%</b> or more compared to the same period in the previous year | Production in the last <b>1 month</b> dropped by <b>5%</b> or more compared to the same period in the previous year     |
|  | Employment              | Employment in the last 6 months has not increased from the same period in the previous year             | No requirement   | Employment in the last <b>3 months</b> has not increased from the same period in the previous year             | <b>No requirement</b>   |
| <b>Benefit level</b>                       | Large sized-enterprises | 50% of equivalent amount paid for the leave compensation  | <b>67%</b> of equivalent amount paid for the leave compensation<br><b>75% if employers do not lay off any employees</b>                      | <b>50%</b> of equivalent amount paid for the leave compensation  | <b>67%</b> of equivalent amount paid for the leave compensation<br><b>75% if employers do not lay off any employees</b> |
|  | SMEs                    | 67% of equivalent amount paid for the leave compensation  | <b>80%</b> of equivalent amount paid for the leave compensation<br><b>90% if employers do not lay off any employees</b>                      | <b>67%</b> of equivalent amount paid for the leave compensation  | <b>100%</b> of equivalent amount paid for the leave compensation  |
| <b>Benefit duration</b>                    |                         | 100 days per annum or 150 days for 3 years  | <b>300 days for 3 years</b>  | <b>100 days</b> per annum or <b>150 days</b> for 3 years   | 100 days per annum or 150 days for 3 years, and <b>April to September 2020</b>  |
| <b>Waiting period for subsequent claim</b> |                         | 1 year  | <b>No waiting period</b>   | <b>1 year</b>  | <b>No waiting period</b>  |
| <b>Application</b>                         |                         | Prior to employment adjustment  | <b>Post-employment adjustment with just cause</b>  | <b>Prior to employment adjustment</b>  | <b>Post-employment adjustment (Jan.– Sep. 2020)</b>   |

Note: Leave compensation for employees remained unchanged at the level of at least 60 per cent of previous average wage to be paid by employers. The table summarizes special measures only for selected crisis; the Government implemented expansion measures on many other occasions. The response to the COVID-19 Crisis (as of June 2020) also includes raising the maximum benefit from 8,330 yen to 15,000 yen per employee per diem for both large-sized enterprises and SMEs.

Source: Japan Institute for Labour Policy and Training 2017; Ministry of Health, Labour and Welfare of Japan 2020b; 2020c; 2020d.



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